RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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**September 8, 1983** **LETTER 869**

Aug. 26, DJIA 1192.07; PTI 1710; A-D Ratio -15.57
Sept. 2 DJIA 1215.45; PTI 1729; A-D Ratio -15.00

**CURRENT MARKET:** In late-July the Averages turned down (see page 1 chart), and on August 8 the D-J Industrials recorded a low of 1163.06. On the decline Transports hit a low of 531.01. A rally followed, and when the Averages turned down again in mid-August the Transports broke to a new low (August 25) of 524.43. Note on the chart, however, that on this slide the Industrials refused to confirm. With the reaction in its third month, this non-confirmation on the part of Industrials sets up the possibility that a bottom has formed.

I am particularly intrigued by the August action from another standpoint. All during June and July the Transportation Average proved to be "the strong Average" in that it did not confirm the weakness in Industrials. Then in August the Industrials "turned strong" in that they refused to confirm the late-August weakness in Transports. When first one Average, then the other, turns strong, such action frequently signals the turn to the upside. I would now say that every day that goes by without bringing new lows to BOTH Averages is a plus for this market (the lows to watch for are the 524.42 Transport low and the 1163.06 Industrial low). Remember, during a primary bull market values are increasing THROUGH TIME. Thus, as time goes by pressure tends to build on the UPSIDE for stocks, and this is the reason why long, dull periods during bull markets are usually followed by higher prices. In a bear market, of course, the opposide is true.

From yet another standpoint, the Utility Average has been acting extremely well, and on the August sell-off the Utilities never cracked below their June 9 reaction low of 126.75. A close of 133 or better for the Utility Average would be bullish for both stocks and bonds.

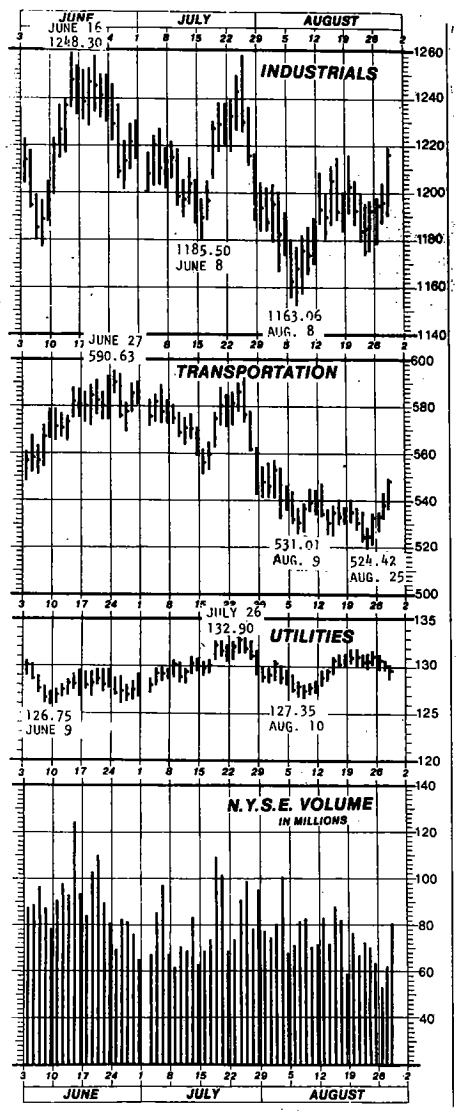
Then we have my proprietary indicator, the Primary Trend Index (PTI). As detailed in the last Letter, the PTI has resisted all the downside action since May. Since May, the entire loss in PTI pointage has been a miniscule 26 points (!) and are you ready for this—on August 30 the PTI closed at its previous high of 1717. On September 1 the PTI closed at a record high of 1721. This is primary bull market action—there are just no if's, and's or but's about it!

The seasonal situation may be of some interest here (although I have never been enamoured by the seasonal approach to the market). October has halted more bear market (and bull market corrections) than any other month. Since most professionals know this, my guess is that we may have already seen the lows (in August) or the lows of this reaction may come in September. Remember, seasonal analysis is simple and easy to understand, and the market loves to cross-up those who follow the obvious.

**UPWARD MOMENTUM:** Some of the best thinking and research in this industry has been done (and is being done) by Bob Prechter, who publishes the *Elliott Wave Theorist,* PO Box 1618, Gainesville, GA 30503. I've frequently mentioned Bob's Elliott work in these Letters. Bob is of the opinion that the market is now embarking on a massive Fifth Wave wind-up to the whole supercyclical bull market—a bull market which he believes started in 1932.

I am including this fascinating chart (page 3) from Prechter's latest report. Aside from the fact that Prechter presents his analysis of the Dow (as interpreted in Elliott terms) going back to 1932, the chart also depicts market momentum. Prechter's momentum index is based on monthly readings for the S & P 500 as a

**FRONT PAGE COMMENT:** Governments, including the US, have expressed "revulsion" and "horror" at the Soviet missile-destruction of a South Korean airliner. But I see the incident as the Soviet's way of telling the world that it can do what it wants with little or no fear of US retaliation. It's another way of saying that whether it marches into Afghanistan or whether it shoots down an unarmed plane, the Soviet military is now so powerful that it cannot be opposed. As I've written so many times, the "shock of recognition" is coming. That shock will be the recognition that the US has fallen behind as a world military power, and I mean fallen behind the Soviets! The implications will be anything but pleasant! (And the reason why I have started a Defense Section will be increasingly clear).

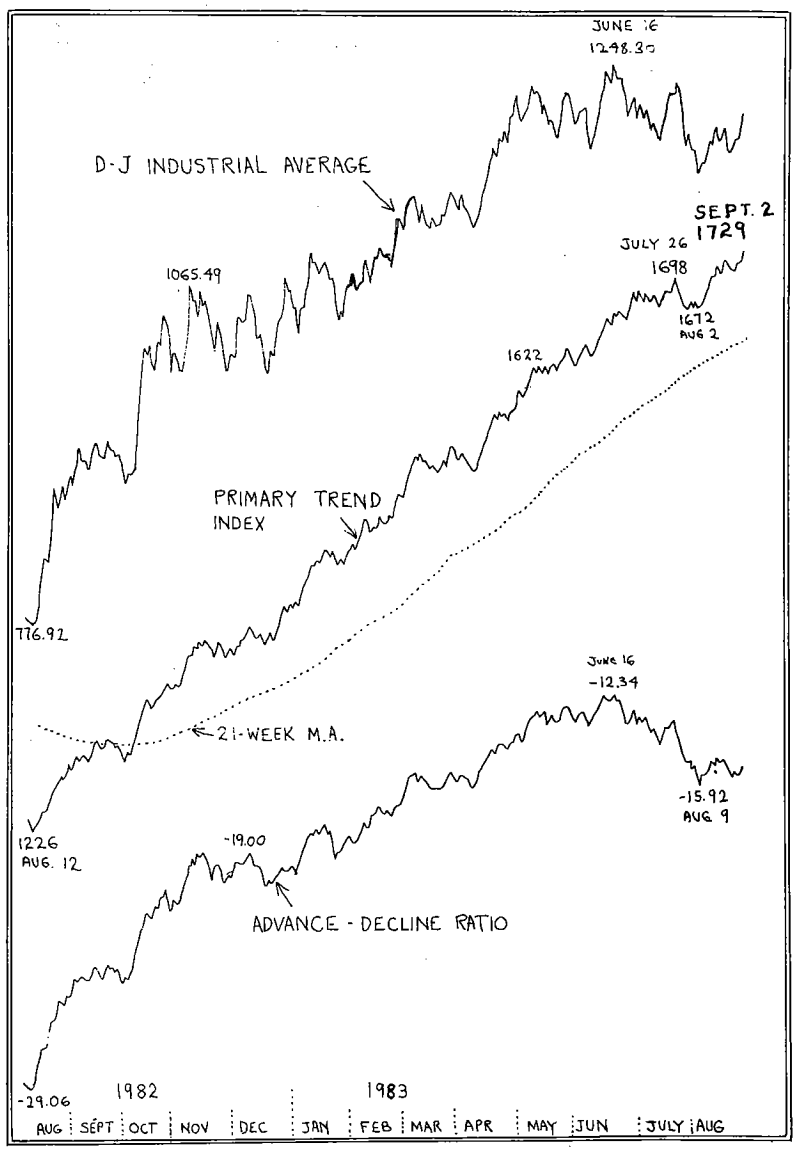


*ratio* of the S & P for the same month one year ago. Due to its construction there is a lag time in this index, and the lag is roughly one year. For this reason, the peak in the momentum index is usually recorded about one year after the upward action begins.

The upward momentum which kicked off the whole 1932 to 19–? super cycle was 124%, an astounding figure recorded in 1933. It is possible that a figure that high will never be seen again. Momentum subsided after the 1933 explosion, but in 1942 the market turned up from the famous Dow reading of 92.92. By 1943 the momentum index had pushed to over 50%, a figure not seen again for decades. The 50% figure served to set off giant Wave 111 of the bull market, a wave that carried from 1942 to 1946.

But this year it happened again! In July, 1983 the momentum figure pushed over the 50% level, this for the first time since May, 1943. Thus, we have recently seen a momentum figure higher than anything seen in 40 years! It is Prechter's belief that the July reading of over 50% has kicked off the fifth and final wave of the great Elliott bull market that began in 1932. Prechter is of the opinion that Wave will carry to the 3600 area somewhere during 1987.

I study this chart, and I ask myself, "Is the situation here in July, 1983 comparable to the situation back in May, 1943 (and I'm talking about the technical situation)." In May, 1943 the Dow was in the 135 area. By July the Dow had pushed up to 145. A reaction set in, and the Dow dropped back to 135 in November. By April, 1944, following a long period of backing and filling, the Dow again touched the reaction low of 135 (this was 11 months after the 1943 momentum peak, and it would be comparable to a low in June of 1984). From the lows of early 1944, the market embarked on a major advance that did not top out until May of 1946 (a comparable advance would carry into the 1986-87 period).



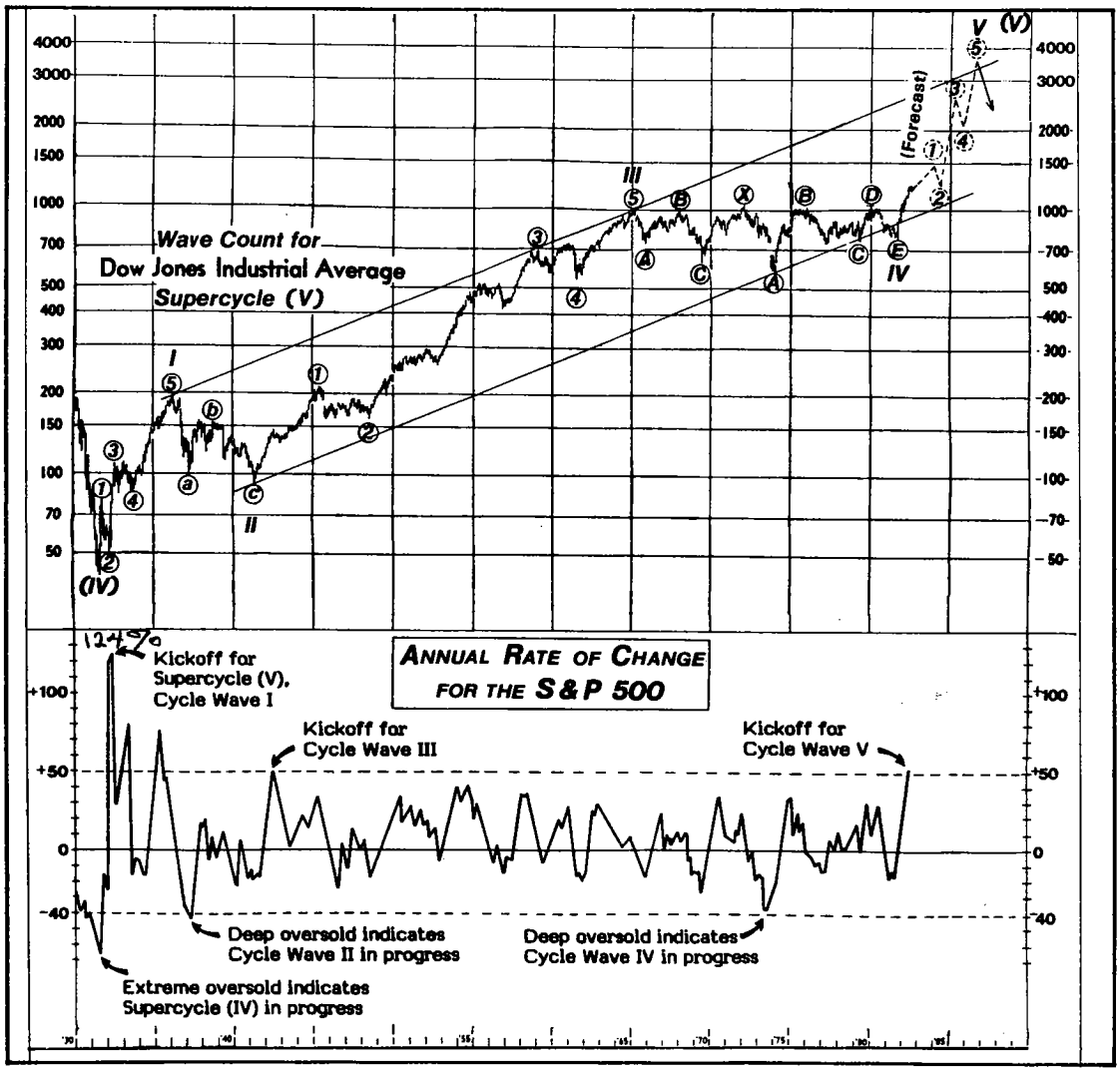

So that's the momentum story. But the crucial thing to remember is that following a momentum reading above 50% (and this has only occurred twice before since 1932) the market has moved up, corrected, and ultimately embarked on a major new advance.

**STRATEGY:** What is the best strategy for operating during a primary bull market? I have gone over this many times, but I want to repeat–in my experience, the best bull market strategy is holding what I term a "fully invested position"and adding to positions during reactions in the bull market. The question may be asked, "What is a full invested position?" And my answer is, "Any position that you feel comfortable with." If you are comfortable with ALL your available money in stocks, then that is your full invested position. If you can only sleep with 50% of your assets in stocks, then for YOU, that is a full invested position.

If an investor moves into a bull market 100%, and he has full faith in the power of the primary bull trend, and he is able to wait out the inevitable bull market reactions, that's fine. But if that same person is invested 100% and he cannot stand the anxiety of holding his stocks through a reaction, then he surely is going to end up dumping his shares at or near the reaction low. So you MUST know your own psyche and your own tolerances. And it is crucial to understand that a "fully invested position" for one person may be something entirely different to you!

One service that generally agrees with me is the excellent Market Logic (3471 N. Fed. Highway, Ft. Lauderdale FL 33305). In a recent issue, this service advocated sitting through this bull market in a fully invested position. They argue (as I do) AGAINST trying to trade the bull market by selling at supposed tops and then buying at supposed bottoms. Says Market Logic, "In sum, selling now with a view towards new buying after a deeper correction involves (1) immediate tax liability, (2) the not insubstantial risk of missing the start of the next rally, and (3) waiting a year to establish a new holding period for long term capital gains treatment. Between these three factors, it will be lucky and nimble traders indeed who will come out better than they would if they had held onto established positions." I agree.

**BIG PICTURE:** Over the years I would guess that I have followed every technique and stock market system on the face of the earth (all right, I'll admit I've missed a few). I've studied cycles, I've gone through the sentiment indicators, the action of the market indicators, I've followed the statistics on the NYSE members, I've used moving averages. And I still follow dozens of




different systems–either on my own or via the dozens of market letters that I receive here each week.

But I'll tell you something, dear subscribers. The most valuable, the most profitable and the surest concept of all is this: a primary bull market can start big or it can start slow, it can last for a few years or a decade, it can produce a few corrections or a lot of corrections, it can be easy to follow or difficult to follow. But in the end it is going to *fully express itself,* and that expression almost always takes the form of *hyper-enthusiam and over-valuation.* Bull markets die in the exhaustion of over-optimism–just as bear markets die in the exhaustion of pessimism.

People ask me, "Russell, how do you know when the period of hyper-enthusiam has arrived?" And I tell them, "You'll know. A bull market that starts as big as this one, a bull market that goes 472 Dow points on its first upward leg, this kind of bull market is fated to produce an almost new level of hyper-enthusiasm before it's over. I can tell you this–we just haven't seen the white heat yet, and we haven't seen the foam and froth yet. I believe this primary bull market is going to end in a burst of extended enthusiasm that will dwarf what we've seen so far."

Now the next question is, "When is this all going to take place?" And my answer is, "I haven't any idea." The hyper-enthusiasm thesis will be IDENTIFIED when it occurs, but there isn't a man alive who can place a time when it will occur. Now I know all about the cycle theories, and I know that there are analysts who attempt to time events down to the months and even the week. But such calculations are usually more fun than anything else. When it comes to accuracy, they have a habit of not working.

For instance, a cycle student may say that three or four of his cycles crest in 1985, so that is the time when this bull market should blow its top. And 1985 comes along, and lo and behold, some bank collapses or Russia shakes her fist or the President has some harsh words for business. So the bull market goes into a severe reaction and the duration of the bull market is extended and the implications of the cycle are wiped out. So the cycle indicates a cresting in 1985, but because of this or that the cycle is skipped, and the bull market is held back and extended.

And that brings up an interesting concept, and this is actually a Dow Theory concept. And it is this: the primary trend can be HELD BACK, it can be manipulated, it can be interfered with–but no force on earth can reverse the prevailing primary trend. The primary trend will run to ultimate conclusion regardless of any and all interruptions. And that is a crucial idea to remember when investing.

For instance, if you study the history of the 1949 to 1966 bull market you will see that it was interrupted again and again. Those of us who lived through that bull market were frustrated over and over as event after event kept the bull market from

(cont. page 5)

# DEFENSE SECTION

Most or all of the defense information (but not stock information) is based on an exclusive arrangement with **Mr. Melvyn Lippman of US Organization Chart Service**, La Jolla, California.

*Building Yesterday's Weapons–for Tommorow's Defense (A US preoccupation).*

*Question:* Mel, I note an urgency in your voice as you explain our defense situation, and frankly it makes me uneasy. Can you explain.

*Answer:* Very *soon,* the citizens of this nation will have to start making some hard decisions about our defense program. The US defense strategy, to put it bluntly, simply isn't working. For the first time in our nation's history the American people will have to determine (with some accuracy) (1) what threats we face to our survival as a republic, and (2) what dangers we face to our economy. As an American, you will need hard facts in order to make these decisions. And unfortunately (almost tragically) these are facts which (for whatever reason) have not been readily available to you up to now. But the situation is over. In each issue of Dow Theory Letters you can look forward to reading relevant military and corporate intelligence data. This intelligence information will make you some of the best informed people in this country. It will also make the tough decisions (which are coming) easier to arrive at.

A short review of three new major weapons systems costing in the aggregate over 90 Billion Dollars will be of real interest and remember these are only 3 out of some 2,000 new weapon systems presently in process.

Profiles:

MX-ICBM, designed to replace the aging Minuteman III ICBM. This new MX missile is 71 feet long, weighs 192,000 lbs, carries 10 warheads with 300 kilotons per, has a range of 8,000 miles and is accurate enough to strike within 100 yards of its determined coordinates (target). 100 MXs are planned and will be placed into the present USAF Boeing Minuteman silos from early 1986 and will be fully operational by 1989.

The Soviets presently have deployed more highly accurate MX-like ICBMs in each of the past three years than are contained in our entire MX program and they are in the process of planning the deployment of a SICBM (small intercontinental ballistic missile) containing one warhead. Our equivalent to this is called the Midgetman and our very earliest deployment date for this missile is sometime in 1992.

ABRAMS - M1, MAIN BATTLE TANK. This weapon system calls for some 7,000 tanks to be built by General Dynamics Corp., Land Systems Division, the current rate of production is about 60 Abrams M1s per month, a total of 720 per year. The M1 was designed to replace the M-60 workhorse tank and will enter full operational capability in 1988. Powered by AVCO Lycomings 1500 HP gas turbine, permitting extremely high acceleration. The Abrams main armament consists of a 105 MM gun which is scheduled to be up-dated in 1985 with the 120 MM long bore gun. The tank carries 40 shells and its secondary armament consists of three different high caliber machine guns. This tank is characterized by high speed, up to 50 MPH, great mobility, high firepower with a first hit capability of 90% at rest or on the move. The extremely hot exhaust gasses from its gas turbine engine make it extremely vulnerable to heat seeking missiles. It burns 55 gallons per hour with a fuel capacity of about 220 gallons. Cost per tank is $2½ million per copy.

The Soviets new T-80 Main Battle Tank is fully operational, has superior composite armor and technology and is being produced with other tanks at the rate of 3,000 per year.

B1-B BOMBER. Designed to replace the 320 older B-52 Stratofortresses, now some 28 years old. Rockwell International, North American Aircraft Operations is the prime-contractor. The B1-B will be powerd by 4 General Electric engines, each with 30,000 lbs. thrust. Manned by a crew of four. The wing span spread is 137 feet and it is 147 feet long and 34 feet high, weighing 477,000 lbs. and can carry a load of 125,000 lbs. of both nuclear and non-nuclear armaments. Its range is in excess of 7,500 miles at supersonic speeds. Cost per B1-B is $230 million per copy.

The 100 B1s called for in this weapons system will cost in addition to the $7 billion spent since 1977, an additional $21 Billion in fiscal 1981 dollars over a multi-year span. Rockwell International will probably place $6 billion in orders with some 3,000 companies throughout the country. At the peak of the production run Rockwell plans to have 8,500 persons working in El Segundo, CA, 4,000 in Palmdale, CA, 7,500 in Columbus, OH, and 2,000 in Tulsa, OK. Approximately 58,000 people, including Rockwell employees are expected to be working on this bomber. The program calls for the first flight of the production bomber to occur in early 1985, and the first 15 B1-Bs to be delivered to the Strategic Air Command in late 1986 and to be fully operational with 100 B1-Bs by 1989.

The Soviets have developed and are now producing several new fighter aircraft, including a new long range bomber. It is manned penetrating bomber with the apparent capabilities of the projected USs' B1-B. The details are sketchy but what we do know at this time is that it appears to be 25% larger than the B1 and nearly 40% larger than the Soviet's current operational Tupolev Backfire bomber. It will have an over-target dash speed of MACH 2.3 (2 1/3 times the speed of sound) and an unrefueled range of 8,400 miles and they call it - Blackjack.

Remember, neither the Abrams Tank, the B1 bomber, nor the MX missile are the results of a demand for new battle tactics. Rather, they are planned and being implemented in the light of current, not future, threat scenarios and to meet the necessity of replacing generations of weapons that had long ago become obsolete.

I have just reviewed three of our future (and foremost) weapons systems. In 1988 through 1992 (these are the years these systems are scheduled to become fully operational) they will be seen as completely obsolete (remember, the Soviets ALREADY have systems that are superior to these).

The defense of the US demands state-of-the-art weapons systems and a dynamic concept. A static concept will be absolutely fatal. This is a grim business, and sooner or later, one way or the other, *the US will win–or it will lose!*

Furthermore, in any battle that may lie ahead–the US must fight with the equipment that it HAS–not the equipment it would like to have.

*(Ed. Note): I hope subscribers appreciate the extraordinary compilation of facts and data which Lippman is presenting*

*here. This section entails a good deal of work on Lippman's part, but he is very desireous of getting the US defense (or should I say lack of defense) story across to my readers. Lippman feels that because of the quality and important positions held by many of the DTLs' subscribers that his defense presentation may have a real impact on the US defense posture.*

blowing its top. There was the Korean war, the 1953 recession, the Eisenhower heart attack, the 1957 recession, the Sputnik panic of late-1957, the 1962 Kennedy panic based on Kennedy's attack on the steel companies, and on and on. Finally, during 1965 and 1966 the bull market died in a frenzy of excitement–and ultimately in a spasm of sheer exhaustion.

So in my opinion our job here is to exercise patience. This primary bull market is still in force, the bull still controls the market, and if my thinking is correct there is much, much more to come. The excitement has now simmered down, a certain amount of pessimism has entered the market, many investors and traders have sold out and are now on the sidelines. This is exactly what the bull wants.

The bull (and subscribers should remember this) is a Wall Street animal, and as such he has a nasty streak in him. The bull wants to rise with as few investors on his back as possible, and by the same token the bear loves to decline while taking as many investors as he can with him. In other words the bull hates to make the crowd rich, and the bear loves to break as many people as possible. And that is why, in a sentence, the stock market is programmed to part the average investor from his money. The minority make money in the stock market and the masses lose. That's the way it has always been, and that (unfortunately) is the way it always will be.

**INVESTMENT POSITION:** Despite dire predictions and much nervousness on the part of investors, this bull market has held up well! As if further proof was needed, just glance at the path of the PTI. Thus, our friend,the bull, continues to grace this box. Hold your defense stocks and hold your no-load mutual funds. This bull market has not expressed itself fully, not by a long shot. This may sound like a shocking statement, but I believe the best has yet to come.

**NOTES & QUOTES:** I don't personally speculate in commodities. But I do follow them, and I am very interested in them. There is no tougher business than trading the commodities, but this segment of the economy is now so huge that anyone dealing with markets owes it to himself to follow the "commods".

My friend Denis Marlow has just come out with a new commodity letter called "Marlow's Major Moves." Denis knows his stuff, and I like his comments and I also like his thinking. If you have any interest in commodities, I suggest you write Denis at Drawer BE, Incline Village, Nevada 89450 and ask for a copy of his latest report.

Incidentally, when I moved out here from NYC in 1961 it was very difficult to operate. The Wall Street Journal was not published here (now it gets here at 4AM), there were no Quotrons or Bunker-Ramo machines, and information was difficult to obtain. Now, you can get it all virtually anywhere in the country. There is literally no disadvantage in living in Panama City or Rapid City or Oswego. It's the new age of instant information, and Denis in Incline Village, Nevada, is getting the same info just as speedily as any broker sitting facing his machine in the heart of downtown Manhattan.

* *

San Diego has recently passed San Francisco in population, and the "City in the Sun" now becomes the eighth largest city in the nation. San Diego has always been known as a "laid-back" city, and it's new mayor, 37-year old Roger Hedgecock would seem to fit in. Hedgecock is a long-term surfer, and he recently ordered a new surf board. The board will have the insigna of the city of San Diego engraven on it. And they call New York "Fun City"!

* *

I continue to believe that the best editorials in the nation appear in the pages of the Wall Street Journal. Here's a piece from a Sept. 2 editorial on the Russian attack on the Korean airliner. And the WSJ is (in my opinion) right on the mark. The Russian policy is intimidation,force, a monster military build-up, and now that they are the number one military power–arrogance. The Russians don't have to answer the question of "why did you do it?" It's done, is the unspoken answer, it's just done.

> We need to ask the next question. Why do we always assume that the Soviets are just like us? Where is the evidence to support such a belief? Would we find it in their slave labor camps? In the imprisonment of Anatole Shcharansky (see Mrs. Garment's column nearby)? In the use by Soviet soldiers of incendiary materials to burn to death 105 Afghan villagers trapped in an irrigation pipe? In the testing of poison gases (yellow rain) on Hmong villagers in Laos and on Afghans?
>
> The die-hard apologists always answer that the American military has done some bad things, too, citing My Lai as a case in point. And indeed, the history of warfare is full of horrors, some committed by people who normally seem quite civilized. But surely we don't need to go into long relativistic debates about man's dual capacities for good and evil to discern that there are crucial differences between the U.S.S.R. and the U.S. On the face of present evidence, one of those differences is that the Soviet Union is fundamentally an armed camp, a place where the regular military and paramilitary KGB hold sway and do not flinch at purposeful killing.
>
> Given our doubts that the shooting down of this airliner was done in error, we must speculate on what high policy aim was meant to be furthered. We know in general that intimidation is central to Soviet foreign policy. The Soviets first aimed hundreds of SS-20 nuclear rockets at Western Europe and then yelled in rage when the West Europeans and the U.S. sought to match this threat with Pershing IIs

and cruise missiles. Through front groups like the World Peace Council they also sucked Western do-gooders into their demonstrations, on U.S. and West European soil, against the Western countermeasures.

* *

Along with hundreds of "special offer" subscription extensions I have also received more personal letters than I ever could answer. Many of the letters were fascinating, and I wish I could reprint all of them here. The extraordinary thing about these letters is that they represent so much experience, and so much authoritative experience.

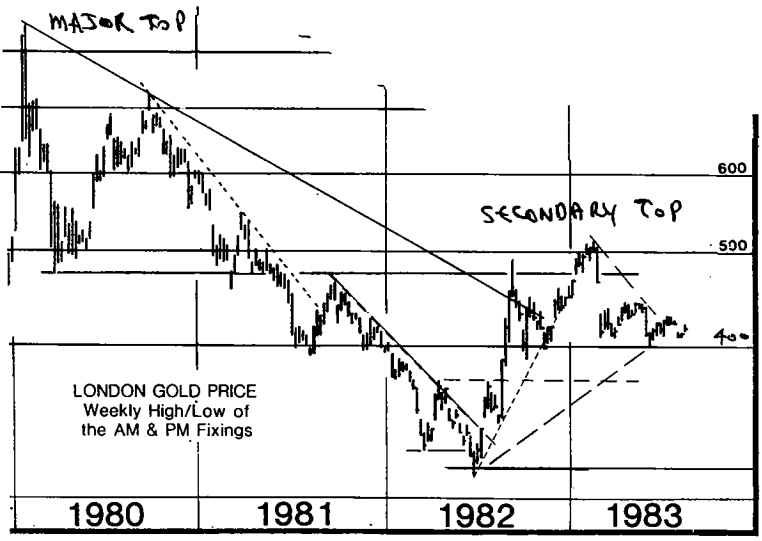
Here is a typical comment: "Your 'Defense Section' is a welcome addition. I am a Navy Commander with considerable experience in non-tactical systems analysis and data resource management. Do you or Mr. Lippman have opinions about which Navy or joint service organizations are leading the revolution in defense strategy? (I've noted that those who are nominally in charge are sometimes oblivious to larger trends)" name withheld.

| | | Our Buy Price | Current Price | |
|---|---|---|---|---|
| NYSE | Harris Corp. (HRS) | 49½ | 36¼ | Defense stock average based on 1 share of each this week is 369 |
| NYSE | LFE (LFE) | 11⅞ | 15½ | |
| NYSE | Planning Research (PLN) | 14⅜ | 16¾ | |
| NYSE | Scientific Atlantic (SFA) | 19 | 17⅝ | |
| NYSE | Tracor (TRR) | 28¾ | 33¼ | |
| NYSE | Electronic Assoc. (EA) | 13 | 13¾ | |
| NYSE | Varo (VRO) | 19 | 19⅜ | |
| NYSE | Bolt Beranek (BBN) | 37 | 73⅝ | |
| NYSE | BDM (BDM) | 43½ | 88 | |
| AMEX | Dynalectron (DYN) | 12¾ | 13⅜ | % Increase is: 32.7% |
| AMEX | Moog B (MOGB) | 15½ | 19½ | |
| AMEX | Systems Planning (SPZ) | 7 | 11½ | |
| AMEX | American Science (ASE) | 10½ | 9⅜ | |
| | Original purchase price 278 | | | |

**GOLD' SILVER:** The latest issue of *Facts* magazine contains an article entitled, "Silver, New Riches from Poor Man's Gold." A number of precious metals analysts are interviewed in the article, and I quote from salient passages in the article. . . . "We're fairly bullish on the prospects for silver for the next year or longer," says Jeffrey Nichols, director of precious metals at J. Aron & Co.

"There is a clear possibility that Silver will double by year end, says James E. Ryan, vice President of National Securities Corp. And here's another opinion: "In the next year or so, Goodman expects the metal to trade between $16 and $18." Finally, "I see prices headed significantly higher," says Smoler, who prefers to look at silver in the long term. He predicts that silver will pass its old $50 an ounce high after 1985."

Well, the opinions are pretty unanimous Silver is headed higher. And from my standpoint, that's just a little too simple. As I see it, the almost unanimous opinion among analysts, hard-money people, magazines and brokers is that (1) more inflation is a guaranteed event, and (2) because of this the metals will surely move higher.




And I ask myself, "If everybody knows this, if it's such a sure thing, why are the markets acting so poorly? Why aren't the metals in the throes of a super-bull market?" And the answer is obvious–there's a flaw in the thinking somewhere along the line. What is that flaw? I think I've expressed it before, but I'll say it again.

The US and world debt structure is so huge, so towering, that the mere act of servicing that debt is deflationary (deflationary because it costs multi-billions of dollars each year just to avoid bankruptcy). In other words, even though the world money supply is going higher, that money is being "burnt up" just to service existing debts. In fact, so basically deflationary is the debt situation that if the money supply simply rose at a sub-standard rate the US and the world would face a deflationary depression.

Here's a weekly chart of gold from the latest report by good friend, Ian McAvity (publisher of Deliberations, PO Box 182, Adelaide St. Sta. Toronto, Canada M5C 2J1). As older subscribers know, I never like a chart situation wherein a major top has formed (as it did in gold during 1980), a major decline occurs, and then on the rally (during 1981 and 1982) a second lower top forms.

And that's where I think gold is now–in a bear market with a secondary top in the process of completion. The critical level is still 400, with gold having to go over 500 to really convince me that a new bull market has been born. In the meantime, gold is sluggish, very sluggish. When the Russian attack on the airline failed to move gold up, even gold bulls must have wondered (if gold was in a primary bull market, it would have exploded on that news).

**LATE NOTES:** Many people were amazed that the market did not "fall apart" on the news that the Soviets had blown an airliner out of the sky, thus fomenting an international incident. But NEWS GOES WITH THE TREND. That is the reason that the stock market shrugged off the Soviet crime, and that is the reason why gold did little or nothing. The trend of the stock market is bullish, the trend of gold is bearish. PTI as of Sept. 2 close 1729---a new high!

**NEXT MAILING: Sept. 21**